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Conference Call Transcript

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PRESENTATION

Operator

Welcome to the Doral Financial Corporation conference call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions will be given at that time. [Operator instructions.] As a reminder this conference is being recorded. I would now like to turn the conference over to your host, Mr. Salomon Levis, Chairman and Chief Executive Officer of Doral Financial Corporation. Please go ahead sir.

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

Thank you. Good morning. We have been a little bit delayed. The bit crowd has already been collected. I'm Salomon Levis, Chairman and CEO of the Doral Financial Corporation. Accompanying me are Mario, Sammy Levis, Senior Executive Vice President and Treasurer and Ricardo Melendez. Executive Vice President and Chief Financial Officer. Thank you for joining us today. The purpose of this call is to help you better understand Doral's 2004 results as described in detail in our Form 10-K and annual report to shareholders. During the course of the call, we may be making some forward-looking statements. We need to caution you that it is possible that our actual results might be different from any forward-looking statements or predictions we make today.

Additional information regarding factors that could cause such a difference appears in our Form 10-K filed on March 15, 2005, with the Securities and Exchange Commission. Before commencing, we are pleased to announce that we will hold investor conference calls in the future to further Doral's quarterly releases. We expect to release our first quarter 2005 earnings around mid-April and look forward to holding a conference call the morning after. As you are all aware, SEC rules restrict the amount of information we can provide beyond of which is publicly disclosed in our SEC filings. If we conclude that we are unable to answer a particular question because of legal considerations, we ask that you do not pursue that line of inquiry. I am sure all of you want to fully comply with the requirements of the Federal Securities Laws.

Before opening the conference call questions, Sammy will briefly address some of the most recent issues being raised by certain analysts. We are aware that many of you would have liked to have spoken to management earlier but we believe this type of conference call is the most appropriate forum to discuss these issues. However, before turning the call over to Sammy, I feel compelled to say that we are very surprised and disappointed at yesterday's market reaction. And certain conclusions regarding our 10-K, that were released without the benefit of management input and before this call. We believe it was premature to reach these kind of conclusions without giving management the chance to react. It was precisely the purpose of this call, to give everyone an equal opportunity to hear management's view on these issues, before reaching their own informed decisions. Now, Sammy will proceed with his presentation.

Sammy Levis *- Doral Financial - Senior EVP, Treasurer*

Good morning and thank you, Salomon. Before I start, I would like to add to Salomon's statement that this conference call were implemented at the request of investors and the same analysts who already have concluded regarding the 10-K before this call. Recently certain analysts have questions. The assumptions that we have used to value our IO's or retaining threads in mortgage loan sales. In particular, certain analysts feel that

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the prepayment assumptions and the discount rates used to value our IO's are too optimistic. We stand by our assumptions and believe that these analysts are incorrect.

Let me explain to you why our assumptions are correct. Prepayment rates used in this valuation of our IO portfolio are determined based on the historical prepayment activity of the non-conforming portfolio on the lines the IO's are judged for management's expectations of their future behavior. Throughout 2004, the nonconforming portfolio experienced continued decrease in prepayment activities. In addition, from the year 2003 to the year 2004, they make-up of our IO portfolio shifted. There was a substantial increase in producing rate IO's, while fixed IO's decreased. The mortgage loan on the lines at fixed rate IO's are conforming loans that have higher prepayment characteristics.

The reduction, in prepayment rates in our nonconforming loan portfolio is due in large part to the strict enforcement of prepayment penalties and the offering of other purchase options to borrows, such as loan modifications and second mortgages, in lieu of promoting cash-out refinancings. It is important to remember that prepayment rates in Puerto Rico have normally run at levels of 75 to 50 percent less of the U.S. mainland prepayment rate. And by the way, these are facts, not assumptions. We expect the discount rate - - the Company determined the discount rate based on 2 main factors; risks and market interest rates. The discount rate use is based on the yield that serve as a benchmark for pre-rating mortgage interest rates.

For several years the Company has consistently used the yield on the FannieMae current coupon as the benchmark and determined the discount rate by adding to that benchmark, a risk premium of 300 basis points. We believe this premium is reasonable, given the low level of historical losses associated with this portfolio. The results shown in the third quarter was basically that we saw a reduction in mortgage rates. The reduction from 2003 reflects the Company's prior practice of using of floor of 9 percent for the discount rate independent of our short rates. The use of the 9 percent floor was discontinued, because management felt such a floor could not be justified in the low internal rate environment. It is important to note that changes in the discount rate will vary with mortgage rates. The rates go up, the discount rate will rise. Conversely, if rates go down, the discount rate will decrease. In other words, the change in the discount rate is market driven.

We will continue to monitor the prepayment and discount rates used in borrowing our IO's to ensure that they are consistent with actual experience. We are committed to providing investors with information by enhancing our disclosure as to how we measure the factors that affect the BIO over IO's. Now we will open this conference for questions. In order to give all participants any questions to participate, the questions will be limited to one per person, plus a follow-up question. After everyone who decides to ask a question has had the opportunity to do so we may open the floor for additional questions, time permitting. First question please.

QUESTION AND ANSWER

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Operator

[Operator instructions.] The first question is from the line of James Allman of Seacliff. Please go ahead.

James Allman - *Seacliff - Analyst*

Gentlemen, my question is for Salomon Levis. If you could please tell us if the board has met to consider a share repurchase program? And if they have not, will you be convening such a meeting in the immediate future to recommend such a share repurchase program? Thank you.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes that's a good question. No, we have not convened officially to discuss this. This is an issue, of course, of pressing results. I look forward to the price action of our stock will help to determine one way or the other. So this is a matter that has not been settled yet. Though of course it's a very interesting, of course it cannot be reported that we have.

James Allman - *Seacliff - Analyst*

All right. My follow-up question is: With your stock off more than 40 percent from its high not that long ago, if the stock does not recover significantly in the immediate future, will you consider selling the Company for a high price to attempt to maximize shareholder value? Thank you.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Let me tell you that we do not have an emotional attachment. You find an investor that will pay like $100 per share. Of course, we will consider it right away. So this is a course of that. If we have an interested buyer to - - of course acquire our Company, it will depend a lot on the price. Right now we are not looking for a buyer, but, of course, if somebody appears, we'll pay serious consideration depending on the price that they are talking about.

James Allman - *Seacliff - Analyst*

Thank you.

Operator

Your next question is from the line of Mark Alpert of Centurian Investment. Please go ahead.

Mark Alpert - *Centurian Investment - Analyst*

Hi. First question is I understand the Puerto Rican governor has proposed a new budget which would increase taxes on the banks. And I was wondering if you could comment on whether that might affect the IDB or other tax status.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

I think they want to tax right now, it's at 5 percent of the net interest income. That's the proposal. Of course, they want to raise the taxes in banking community and insurance companies, broker bureau corporations and other finance related companies. They total $190 million in the next 2 years just to cover the deficit. Of course this - - these are some ideas. We have the legislature that is controlled by the opposing party. I think we can get to a situation of operations and it's something we will have to pay. But now the maximum there, now the proposal - - I'm sorry, by the Governor, mentioned last night was 5 percent tax on the net interest income for banking institutions for the next 2 years until we have a reform on our tax laws. And of course, our business is at this point.

Mark Alpert - *Centurian Investment - Analyst*

Okay and then my second question is, could you describe how the hedging has changed between year end and today on the IO strip?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, we have the blessing of our Chairman Greenspan that he mentioned that we - - the interest rates especially long end of the curve, were not headed in the right direction. And he called it a conundrum. And of course a short-term aberration. I think after he spoke, the 10 year has increased dramatically from a low 3.98 yield to 4.57 percent in a matter of 4 weeks. Of course, we have a situation announced yesterday by GM that they expect to have a loss and is a very important Company in the U.S. and we have the airlines. And we are all going higher to raise a new high. And we have to see what the impact will be in the next few months. I think today, the micro was riding a little bit in the treasuries. And also it happened last year when we had the so-called soft crash. And we have the inverted - - not inverted the flattening of the curve that has lasted for a few months in the second half of the year 2004. Of course, also we have to see the kind of appetite that the floors at our banks will have on U.S. securities. In January it was very high. The kind of purchases of U.S. securities conducted by Central Bank. But this happened in January we are now in March so we don't know. The market is a little bit uncertain, but it seems that the economy will tell us - - if it is fair we will continue price ceilings as a strengths or are we going through another patch. Or we maybe going through a situation to slow down the economy or, because it seems to be that all prices is - - maybe not of this price. If they go even higher than they are it could become like a special tax on consumers.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

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Mark, if I may add to that, there was in the 10-K an old saying that after December, we have our new hedges in order to protect our interest assets including the IO. And if I may go back to the question of the government, proposing a tax, bear in mind that the government is inviting the private sector to discuss it and find the most efficient. And as a matter of fact, we happened to have our president, Zoila Levis, who is now the President of the Puerto Rican Banking Association, that will closely monitor these. And actually, the newspaper, the Treasury Secretary - - I'm sorry. He actually mentioned that probably would most likely will be a tax of interest earned between 2.5 to 3.5, right in that 5%. So it will be probably more towards that - - those 2 numbers. And only on interest. And bear in mind that our Company has a lot of interest income that is taxed semiannually.

Mark Alpert *- Centurian Investment - Analyst*

All right. Thank you.

Operator

Your next question is from the line of Jordan Hymalach of Philadelphia Financial. Please go ahead.

Jordan Hymalach *- Philadelphia Financial - Analyst*

Hi. I just have 2 quick questions. One, I understand that your loans are sold with full recourse, is that correct?

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

No, as a matter of fact, today most our loans are sold with no resource at all. In some cases there's recourse, but of a limited measure. Meaning some have recourse of up to 2 years and then that goes soft and some of them have a limitation of 10 to 15 percent. But, however, you know that portfolio which has 60 percent loan to value, which charge-offs almost non-existent. I mean, the credit risk of that portfolio is almost 0.

Jordan Hymalach *- Philadelphia Financial - Analyst*

So other than REIT's and warranties, it's not sold with full recourse and so hence the buyer does not have the right to put it back to you?

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

The majority of the loans are not sold with full recourse.

Jordan Hymalach *- Philadelphia Financial - Analyst*

Okay. And second question, in your 10-K you mentioned that - - and I will read the exact wordage. The increase in the adjusted rate loans from 2004 compared to 2003 was due to the purchase of $200 million in adjustable rate residential mortgage backed loans from a local financial institutions. It continues. In a separate transaction the Company sold $200 million of first and second residential mortgage loans a gain of $24.8 million was recognized during 2004 as a result of such sale. In RGFs 10-Q it says the exact things but almost revers. My question is: assuming that the buyer and seller is RGF why are you buying and selling loans from RGF or somebody else and recognizing a gain? Can you describe this transaction a little more?

Sammy Levis *- Doral Financial - Senior EVP, Treasurer*

Well, these are 2 type of different portfolios. The one that we sold is residential, and fixed rate and the one that we purchase are going to be on a floating. As a matter of fact, these loans are going to be paid to us on a floating basis. In a way that's a hedge to our IO. But these are 2 type of different types of portfolios. And also, we are selling also commercial loans and second mortgage loans that we cannot [inaudible].

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Jordan Hymalach - *Philadelphia Financial - Analyst*

Okay. Thank you.

Operator

Your next question is from the line of Randy Sealec is Isenbach Capital. Please go ahead. Please go ahead.

Randy Sealec - *Isenbach Capital - Analyst*

Hi, gentlemen. Question regarding your IO's. Can you explain how you've changed your hedging to handle non-parallel shifts in yield curve? And what the likely that you'll be taking additional IO writedowns will be in the future? And what kinds of caps you have in place? And then lastly you know you have a lot of cash on the balance sheet at 1 plus percent. What are you planning on doing with that? Are you going to redeploy that any time soon?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Of course, we have been waiting for the rates to go even higher. And, of course, again, most of them may be wrong because economics were running 2003 and 2004 and maybe again we are wrong in 2005. Of course so far what we have experienced an parallel shift in rates especially after we experienced a steepening of the curve. And what we have is hedging on all sides of the curve. Short term, medium term and long term. The best way for our hedges to work is when we have the parallel shift. So even with a shifting in only short term, we are, of course, protected. But the best way to be protected is a parallel or a steepening of the curve. And that's what we envision will happen in light of the comments by Chairman Greenspan in which he mentioned the options. I'm sorry the long-term rates were extremely low. So we have an options for instance on Euro dollars. We have intra-rate caps, intra-rate swaps that also of course, they will help us in a case of rate continuing to go up. And please refer to page 39 of the annual report in which we envision the gains that we will have in the hedging portfolio.

Randy Sealec - *Isenbach Capital - Analyst*

Got you. What about the possibility of taking significant additional write-downs of your IO's. Do you think that's behind you or --?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Of course it is - - that would depend on - - if we - - if you again, go to page 39 of the annual report, you will see the - - that we are one of the 2 companies - - we clarified or we put that in writing so clearly. So go to page 39, the kind of sharks that we'll have with 25, 50 basis, 100 basis and 200 basis what will happen to the valuation of our IO's, even with the PSA that remains stable. And also the changes in fair value in our hedging. So one thing will compensate the other, if everything works the same. We have the 200 basis points, we could lose like over $500 million in IO's but we could recoup like over 500 million also in hedging. So that's something, of course, that's why we have hedging in place. So we feel that this is a significant portion of our losses will be covered by hedging. By the way, that table - - bear in mind that the changes in the fair value, was sufficient that we had in hedges as of December 31. You know in that same table, we note, as I said before, that the Company has entered into a new [inaudible] instrument to protect the value of its IO after December 31. So although you can see the - - how one affects the other one, you have to take into account that now there are others and new positions that we are after that they want done.

Randy Sealec - *Isenbach Capital - Analyst*

Okay. And what about the caps that are in place to prevent losses beyond a certain point? Can you describe those?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Well bear in mind that these caps - - by the way, these are actual caps in the contract of each agreement. All of them has been negotiated with all of these - - with the many institutions that we sell loans on a one-to-one cases. So all of them vary there's no - - I mean, they are not similar. Each

of them differ. So - - I mean, we have included some generic disclosure on the use of cash in the same case but providing us a specific rate is difficult because there's no uniformity. The cash varies from buyer to buyer in negotiated contracts. And also for competitive reasons, we can't disclose where those caps are. Because in some cases, with one institution they may be lower and another is higher. That could also have a negative impact in - - or a positive impact in those institutions. So we just don't want to share that specific item.

Operator

Your next question is from the line of Jay Cunningham of Southcoast Capital. Please go ahead.

Jay Cunningham *- South Coast Capital - Analyst*

Good morning. Thanks for the call. Let me see, I've got a whole list of these things here. Why don't we just go down and why don't we just walk through, if you will, all of the components of the gain on sale margin and all of the then corresponding margins that you realize, you know, including both the IO and all the other components?

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

Yes, I will refer this question to our Chief Financial Officer, Ricardo Melendez.

Ricardo Melendez *- Doral Financial - Exec. VP, CFO*

Yes, good morning. the gain on sale is composed of several things. We have on gain on sale, fee income. We also premium and discounts on sales of loans in the cash window and in the market. Also the gain on sale has the capitalization of the mortgage rights. Which as we disclosed in the 10-K basically range from 150 basis, to 120 basis more or less for capitalization. The higher rates are for the FHA and the conforming. Most of this is in Puerto Rico and the lower rate for the nonconforming. In addition a significant component on the gain on sale is the capitalization of the IO, which as we disclosed in the financial statements, it's based on our expectancy of the future cash flows. Also the [inaudible] that we are reporting. Essentially speaking we are doing [inaudible]. Basically it is composed of the cash flows that we're going to receive in the future, discounted - - at discount rate. Sammy explained how we obtain the discount rate at the beginning. Which the discount rate is in line with the yield that we're expecting on the IO. In addition, to that we use prepayments assumption which is based on the most recent historical prepayments fee with our expectation of how the portfolio is going to behave in the future.

Jay Cunningham *- South Coast Capital - Analyst*

So if I'm looking at this, in your - - the assumptions that you set forth, both at year end '04 and then year end '03, you were using prepaid assumptions of roughly 18 percent in '03. So I guess my question is: was it that reality, which Sammy seemed to indicate early and then if so, then if you quantify what the total revenues were from the prepayment penalties that you realized in '03? I guess conversely then if the 18 percent was not reality, why the dramatic change from today versus a year ago?

Ricardo Melendez *- Doral Financial - Exec. VP, CFO*

No, the 18 percent was reality. The composition of this portfolio has changed. It seems 2003 by a lot right now. The underlying is supporting the IO. The viable IO has more than doubled when we compare that number and also the prepayments in the portfolio are going down compared to the levels that we have in that prepayments beginning 2003. [Inaudible] That is lower and, of course, you know the prepayment in the portfolio are reduced. Also when you say on the prepayment penalties, usually the prepayment penalties are established based on the percentage of the loan and that is percentage was 4 percent and this goes down to 4 or to 1 percent. There's a prepayment penalty in the first year of the loan up to the fifth year of the loan. After the fifth year they don't have any prepayment penalties. And the income originating on those prepayment penalties is around over 500,000 term loans.

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

I would like to add that according to information provided to us by stock analysts, the prepayments speed in the U.S. also varies tremendously. For instance, they reported to us that Wachovia prepayments in 2004 was 41 percent, while Wells Fargo was 14.9 percent. And in Puerto Rico Fannie Mae, we are running at a speed, Fannie Mae that's agency have 40 percent, 50 percent maximum of the PSA's running in the U.S. as an average. So we are probably 30 percent, to 14.9 percent of Wells Fargo that seems to be that they a business similar to ours. And it would be the same point as 2 percent that we have on the books. So we are running, you know, parallel to the U.S - - and of course in the U.S. you have companies that have associated big prepayment like Wachovia, even CountryWide and others like Wells Fargo, that it is also one of the largest - - even the largest in mortgage lending, they have prepayment fees of only 14.9 percent.

So there are different experiences depending on different lenders, different areas of the U.S.. And, of course, our portfolio is composed primarily of low balance loans. So the prepayments are lower and we, of course - - we don't have any incentive now for our market force to go after these loans of 3.9 percent. Because many of these are refinancing and refinancing business is driven by us, by the Company. Looking for more business on plans. So anyway, we feel comfortable that this is something that we'll to stick to as the rate continue like that. Of course, when we have to pass on 3, but we have the so called disinflation, and, of course I think went as low as 3.11 percent, in the middle of the year in 2003 and with the inflation of our job we have bigger prepayments. So I think it's variation of our base and the experience that we have in Puerto Rico vis a vis the U.S..

Jay Cunningham - *South Coast Capital - Analyst*

So I'm sorry, but Ricardo, I didn't catch, did you quantify what the prepay revenues were in '03? And then could you clarify the change in the composition?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Yes, the prepayments - - the prepayments revenue was 6 million per year, more or less in that range. Obviously that is increasing every year because we are increasing the portfolio so we expect that number to go higher. What was your other question, please? You said the composition of the portfolio has changed. Can you give a better color around that?

Jay Cunningham - *South Coast Capital - Analyst*

Well, yes. Obviously, the portfolio has chipped into our nonconforming mortgages right now which basically for us is the most problem. And also with the balance on the portfolio has gone down from almost 7 percent [inaudible] that we had 2002, in the range of 600 - - 65 right now. And that tends to decrease the prepayment speed because we're not likely to refund them since they are already at lower rate. And then can you give the percentage breakout then?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

It is a 50 percent - - relatively speaking on conforming and 50 to 60 percent on conforming and 40 percent on conforming.

Operator

Your next question is from Joe Gladue of Cohen Brothers. Please go ahead.

Joe Gladue - *Cohen Brothers - Analyst*

I guess most of my questions on the IO's and the hedging have been answered. But let me - - I know earlier in the year, a number of insiders had been doing some buying. Plans to continue that?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Bear in mind that we can't comment on that. And also remember our policy that we are in a blackout period 30 days before our earnings. So we -

Joe Gladue - *Cohen Brothers - Analyst*

Okay. Thank you.

Operator

Your next question is from the line of Graham Tenaka.

Graham Tenaka - *Tenaka Capital Mangement - Analyst*

Yes, I was just wondering if you could give us your end depreciation rates, say in each of the last 5 years, just to see what the variance has been either in the industry or your experience?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I'm sorry, can you repeat the question?

Graham Tenaka - *Tenaka Capital Mangement - Analyst*

Yes, I was just wondering what the actual prepayment rate, the fee was over time? And so if you could give us - - I hope have you the data for either the prepayment rate averages in Puerto Rico or in - - for Doral, for each of the last 5 years?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Well, if we go back to 2002, in 2002, there were payments - - we have prepayment fees of 250 PSA's. In 2003, the prepayment fees went up to 337 PSA and in 2004, we saw that fees went down again. We look at these every month specifically and we adjust our prepayments estimates based on the historical prepayment fees that we experienced in the portfolio. Also, you have to take into consideration - - for example, the prepayment speed that we are disclosing on the financial statements is the prepayment speed that is combined on the portfolio. In order to solve this we decompose that prepayment speed by portfolio. And this is not information that is released. But the prepayment speed that we use for the value of the IO is based on the IO portfolio and not on the overall portfolio as a whole.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

For instance, this is Salomon. To give you an idea, mortgage reported in the year 2000 that prepayment went from 7 percent to 25 percent in the same year period experience, a 7 percent prepayment rate to 25 percent.

Graham Tenaka - *Tenaka Capital Mangement - Analyst*

I also was wondering, you were talking about the prepayment rates relative to how fast a disincentive for people to prepay or to refinance, the cost of refinancing for the average customer and relative to what size portfolio?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, that's a very good question. Puerto Rico is very different from the U.S. in that sense because in Puerto Rico, doing the refinancing transaction there are certain costs for the borrower So it's not our practice to refinance. For example, like in the States you can see heavy refinancing going from 5.75 to 5.50. You don't see that kind of refinancing of Puerto Rico because it's not our practice based on the costs that you have to pay. Which are basically paid by the borrower they are not assumed by the lender.

Graham Tenaka - *Tenaka Capital Mangement - Analyst*

And roughly how much does that cost on average?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

On closing costs, it will depend on 2 to 3 percent, depending how much the notary fee will be. Because the notaries in Puerto Rico, public notaries, they have to be lawyers. Right now, they want a minimum fee of 1 percent. Of course this has not legislated yet. And then looking for a minimum of 1 percent fee of the total transaction. So I would say from 2 to 3 percent. In addition to that prepayment penalty, that could run to 4 percent or 3 percent, depending on the hedging of the loan. So it's all in all I think you could leave a 1.5 point. I remember in '93, when I personally called some customers and I told them listen you will be saving $35, a month. They said no I don't care for that amount. You give me a bigger resorption a will come back to you. So I would say as a rule of sums you will need like two percentage points lower for people to be driven by rates if the loans are, let's say 150 and up. Because for small loans like $25,000, $35,000, $50,000, it doesn't pay for a borrower. Unless they get a cashout. A cashout is all right for them. But we are doing a person a customer a - - mortgage borrower they come for refinancing, we will end up giving a second mortgage.

Graham Tenaka - *Tenaka Capital Mangement - Analyst*

You are saying you need mortgage to be 2 percent lower to make it worthwhile for the current mortgage - -?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes. Yes. Depending on the size of the loan. If have you a $1 million loan, of course maybe you could live with 1.5 point or 1.25, but our typical customer is anywhere from $25,000 to, let's say $100,000. Also, you have to know in Puerto Rico, the majority of the refinancing activity, as most of you may know, is driven by consumer consolidation of debt. So that happening in cycles every so often, not every time rates go down. That's one. The other thing - - I think this is very important. The success of Doral mortgage banking is our aggressiveness in marketing. And we are not pursuing this client and one of our marketing person know that this client sees not much refinancing be done. So we can't decrease that significantly. We said before, the- - there are other priorities that the client may have instead of a refinancing. Thank you very much.

Operator

Your next question is from the line of Steven McBoyle of Lord Abbott. Please go ahead. Mr. Boyle your line is open.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes. Yes, we're here.

Operator

Yes, do you have a question, sir?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I think he's probably not in the line anymore.

Operator

Okay. Moving on, your next question is from Wat Webb of Oakwood Management. Please go ahead.

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Wat Webb - *Oakwood Management - Analyst*

Hi, Sammy, hi Salomon. Gentlemen, you know, I have read the 10-K, as I do every year. And generally speaking, I'm perfectly comfortable with the way you guys have been running the business. As I have been for years. But, you know what is different now because of the hysteria that has been generated around the gain on sale issues, et cetera, I really think you owe it to us as shareholders - - I don't know that you can give us a date, but to come back to the very first question. I look at a Company that has a very high ROE that generates massive amounts of capital every year. That's massively over-capitalized and I say, there's plenty of growth capital being generated every year from earnings. And again, I just -- I would like you guys to seriously consider giving us a date or somehow responding to the issue of the massive share buyback and a substantial increase in the dividend in the near future. I just think you owe it to us at this point.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

We'll have the next conference call for mid-April and then we'll have more information for you. But of course the lower the primary goal the more attractive it becomes to the board to authorize this. Unfortunately we cannot give a date. But mid-April, we can revisit your questions and try to answer it more precisely.

Wat Webb - *Oakwood Management - Analyst*

Excellent. Thank you. One little follow-up. You know you mentioned - - I think Sammy had given me this information before. But is it possible to divulge to us or even publish some of those - - you know how you get 2 outside opinions on those valuations. You mentioned it more than once in the 10-K. I was wondering if it was possible for you to divulge who those firms are and perhaps publish some of those outside valuations just to give us some extra comfort?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, these are 2 reputable firms. firms. We have signed a confidentiality agreement with them and we just can't disclose their names. But all we can say is these are well known and very reputable financial firms.

Wat Webb - *Oakwood Management - Analyst*

Okay. Thank you very much, guys.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes.

Operator

Your next question is from the line of Ken Bruce of Merrill Lynch. Please go ahead.

Ken Bruce - *Merrill Lynch - Analyst*

Thank you. Good morning. In light of some of the questions that have been asked and obviously some of the controversy surrounding the IO securities, has there been any serious consideration given to possibly selling these IO securities and monetizing the assets which would certainly free up some of the capital that I think is probably restricting you from doing A share purchase?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

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That's a good idea but these IO's are not so liquid as the trade securities. So this is something that in the past we have done it. And that's a good idea but they are not as liquid as other components of our asset portfolio. Also, remember that we are receiving a significant spread on our IO every month. So the IO is really producing for the cash for the Company. Right now, the notion, more the mortgage line of the IO roams around $7 billion. And we're retaining the spread on that $7 billion dollars which is a significant portion of cash for the Company.

Ken Bruce - *Merrill Lynch - Analyst*

I recognize that these are obviously fairly high yielding assets for the Company. But just given that they are causing so much volatility, in terms of people speaking about the shares and the Company's earnings power in general, it seems to me that you can basically maybe have some of these outside parties put real numbers on the securities and ultimately monetize some of the assets without materially weakening your cash flow generation capabilities but at the same time supporting the valuations that you are basically putting on them internally.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

What Ricardo mentioned is that this is like a cash cow, you know. For instance, we are running $167 million in cash, received from the IO's to give you a return of over 20 percent. But something that we have - - the net income also could be affected with the disposal of these IO's. Any ways it's a situation that we can consider going forward, depending on what is the best course of action for the Company.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Well, definitely these IO's, it's a good cash income for us.

Ken Bruce - *Merrill Lynch - Analyst*

I guess one followup is: could the Company provide some specific detail about the IO's securities themselves so that outsiders can better understand what the economic value might be independent of the 2 very general valuation parameters that you provide today? It seems to me that gross spread and some other particular characteristics about the IO's will be quite helpful for outsiders to try to arrive at maybe what the value is independent of your internal valuation.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes, we believe that we have provided significant disclosures in the 10-K. But it you have any suggestions, please feel free to submit those suggestions to us and we will gladly evaluate the suggestions and determine if we can add additional disclosures in our future filings.

Ken Bruce - *Merrill Lynch - Analyst*

I will. Thank you.

Operator

Your next question is from the line of Nick Van Brokhoven at Lafoyer Assets. Please go ahead.

Nick Van Brokhoven - *Lafoyer Assets - Analyst*

Yes, all of my questions - - first of all, I want to congratulate you on a good job managing this Company and I know the stock price is not reacting favorably. It's trading down 14 percent again now. I'm just wondering if the press releases that have you been releasing after the Hibernia SouthCoast report, and the SEC investigation into W Holdings, the - - do those 2 statements still hold?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

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Yes. I mean, we have no SEC investigation at all on any matter.

Nick Van Brokhoven - *Lafoyer Assets - Analyst*

No. No. But I was referring to the W Holdings and after that you said that you weren't investigated and you weren't having any - - all the issues that W Holdings had.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I -- I -- The press release stands today. The press release stands.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Yes, of course.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Of course.

Nick Van Brokhoven - *Lafoyer Assets - Analyst*

Okay. And then I was wondering in your response to the Hibernia report, I don't know, 2 weeks ago or something, you said that you stand by your guidance and you think that the analyst estimates are just way too low. Do you think that's still accurate today?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, our policy is not to comment on earnings estimate or to provide earning guidance. If we make an exception to the policy we will do so through a press release. We can tell you that the (inaudible) for our business are very strong. We are anticipating for the first quarter of 2005, record mortgage production, record commercial loans and record PE income from insurance agency. We encourage you to participate in the next investor conference on April the 15 on the release of first quarter.

Nick Van Brokhoven - *Lafoyer Assets - Analyst*

Yes, but I'm just referring to the last sentence of your reaction to the Hibernia report, issued on 8 March. And it says exactly the Company has previously said that it expects to meet or exceed the consensus earnings estimates. So we belive the analysts' estimates are unrealistic. I'm just wondering if you stand by that statement.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Okay. That came out from a public investor conference call in New York, several weeks before that. We were in that investor conference that we saw for the quarter. we say that we were expecting to meet consensus estimates. We stand by - - for those statements that we make publicly at that time.

Nick Van Brokhoven - *Lafoyer Assets - Analyst*

Okay. Thank you very much.

Operator

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Your next question is from the line of Charlie Ernst of Sandler O'Neill. Please go ahead.

Charlie Ernst - *Sandler O'Neill - Analyst*

Good morning. I just wanted to ask a question about the nonconforming loan sales and the policy of putting caps into the sales. How much of the nonconforming loan sales actually carry the caps?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Basically, all them have a caps.

Charlie Ernst - *Sandler O'Neill - Analyst*

So you are saying that the buyers are the ones that are actually holding the rate risk?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

They are holding - - it's just that we will pay them at some moment, when it continues to go up. At some moment that we pay [inaudible] and is going to be capped. So - - I mean, those caps will really protect us and it's for this IO asset never to be in negative - - to have the ability to split.

Charlie Ernst - *Sandler O'Neill - Analyst*

Again that does imply that the buyers under this structure are the ones that ultimately are holding the rate risk because you all —?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

If the IO goes up significantly higher, yes. But by the way we do understand - - I don't know why this will be a factor. They like some type of hedges in order to protect these caps.

Charlie Ernst - *Sandler O'Neill - Analyst*

Okay. And then in the transaction that was talked about earlier, the loan sales back and forth with R&G. Instead of buying loans from R&G that were floaters why wouldn't you just use some of your originated fixed rate loans and then swap out the rate risk?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, they give us a higher rate because they are higher of the market. And in turn, we can sell them loans that right now we're going to sell to other investors. I - - and also bear in mind that these loans are repurchased on a floating basis. They are Puerto Rico loans and we need the assets in Puerto Rico.

Charlie Ernst - *Sandler O'Neill - Analyst*

Okay. And my last question is: Are there actual qualified opinions from your accountants on these loan sales in terms of whether they are final sales?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Well, technically speaking, they are accounting rules in effect allows to recognize these contributions of the sales and to recognize the MSR's in [inaudible.]

Operator

Your next question is --

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

By the way - - by the way, let me add to that we do have [inaudible] opinions.

Operator

Your next question is from Tom Purcell of Viking Global. Please go ahead.

Tom Purcell *- Viking Global - Analyst*

3 questions. The first is just on the RGF sale. The gain that was recognized in that sale was that a cash gain or was that a non-cash gain on sale that was recognized?

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

That is basically a non-cash gain. The present body of the retainings that were created in the sale.

Tom Purcell *- Viking Global - Analyst*

Why were there retained interests created - - I guess that doesn't make a lot of sense to me. If you bought the floaters from RG, and sold mortgage loans at I guess a 12 percent gain is what it looks like. Were these transactions done on the same day and were they related to each other?

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

No. The transaction were independent one of the other in the complication of the loans that RG signed they have different characteristics. So - - really they are different transactions and they are not related. They were the same type of loans that [inaudible] So they are different. It's completely 2 different type of loan. Of course, these to R&G are minimal percentagewise to what we do in the market. We have invited other people to sell those they don't want to sell. Because they don't have the production sometime and they want to keep it to only production. But I'm afraid that [inaudible] bear in mind although they are a floating in the very beginning, the cap is much higher than the existing current rate. For instance, the general rate in the last few months was 5.5 percent on a 30 year mortgage and we were getting 6.25. Of course that will give you a hedge of 75 basis points and on top of that you can buy a cap to protect for any significant higher amounts. All in all I think it's a good business for us. Because we are protected. We can buy some caps that are very inexpensive. The 6.25 caps that were very inexpensive for 5 years. We have the best of 2 worlds. We have rising rates in the short term rates. And we can take caps that are much higher than if we enter into a 5 percent Fannie Mae security, for instance, at that time that we are trading [inaudible.] By the way, I need to say that these loans, bought from R&G, were bought from the Bright bank. The Bright bank is [inaudible] And from time to time, they need to acquire a - - assets in Puerto Rico. The Company cannot sell our loans to our bank. So they, as other institutions, buy loans from others and they are also doing the same thing and for the banks it make sense to buy those on a floating basis. This is Dorel Bank not Dorel Financial.

Ricardo Melendez *- Doral Financial - Exec. VP, CFO*

I also want to add that although we have - - part of our income is non-cash through 2004 approximately 1/3 or 150 million was cash income. Okay. I will just have to follow up with you. I can't say I still understand why there would be a gain on this particular transaction. I have another

question. Looking at your 10-K, it's scheduled - - sorry, Table J. You buys just related to the servicing portfolio you actually put in there your actual CPR's, which reading from the schedule in 2002, '03 and '04 were 14%, 17% and 15 percent respectively.

Tom Purcell - *Viking Global - Analyst*

If on your actual portfolio, that's the CPR, why when you set up the gain for the IO, are you using CPR's for the servicing rights of 9.4 percent and for the IO's it's 7.2 percent which are significantly lower than at least based on Schedule J, your actual experiences in the last 3 years?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Okay. It is the CPR that I disclosed in February is a the historical CPR for the entire 2004 on the whole portfolio. The CPR that we use in the assumptions to value the MSR's and the IO's are based on the most recent CPR historical data that we have specifically fourth quarter '04; adjusted for the expectation we have we have into the future. And that's basically why those 2 numbers are different.

Tom Purcell - *Viking Global - Analyst*

Okay.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

So this is - - the reason the CPR has dropped so much is that basically that you are just - - I guess you are just expecting CPR's to fall 8.5 in '05? Okay.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes. That's what we have seen. It's not an expectation, it's what we have at December 31. If you look at the CPR's, in years, you'll see that there's a downward line. Basically, as CPR's we saw that they were decreasing. We are anticipating that they going to be lower in 2005. By the way, the CPR translating to a PSA, prepayments penalty of about 120 percent. We believe we can sustain this rate for the foreseeable future. We know that during the early 1990s, Dorel's financial issues for CMO's, with similar mortgage loans that were sold as our existing nonconforming. Generally, using at that time a PSA of more than 100. Even a lesser PSA. And it's where CMO's that were issued in the 1990's. During the 1980's and '90s, I mean the year 2000, PSA in Puerto Rico, were in fact very low. Historically, [inaudible] it was significantly below that of the U.S. national average. So, you know, even at that time, we even had lower CPR's.

Tom Purcell - *Viking Global - Analyst*

One last question which is on the hedging. Just reading table E from the 10-K, your derivatives which are presumably used to hedge. You gad you losses in 2002, 2003, and 2004, despite different rate environments in those years. And then looking at the language that you referenced earlier, from the table from page 39 that had the changes in the IO's. if LIBOR increases by 25, 50, 100 or 200 basis points. And then looking at the language around the securities value changes, it looks to me like you guys are hedging the long end of the curve, while your exposure on the IO's is really to rising LIBOR because you basically have an inverse IO. So why, if the exposure is to rising LIBOR, why aren't your hedging the short end of the curve rather than the long end of the curve?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Now we are actually. I mean bear in mind that hedges were put in place to protect our Company in a rising interest rate environment, assuming a better issue. Meaning as short term rates to go up and long term rate to go up. In this last quarter, only short term rates were the ones that went up and nothing happened to the long end. But now the Company has done some adjustment to protect more against the - - if long term - - if all rates, short term rates and long term rates would have gone over the same time, or even if it was less you know, the hedges would now work more efficiently. But now we adapting at those hedges to take more of that type of environment. Yes, but your view in 2004 numbers is correct. That's precisely was there a reason why we have impairments in the IO and at the same time not on the hedges.

Tom Purcell - *Viking Global - Analyst*

Okay. Just one last question on this changes in the value to the IO's. I thought when you sold these private placements, securitizations to other banks in Puerto Rico that had you caps. And as I read the language around that table it says, it summarizes the estimated change in fair value of the Company's IO's net of imbedded caps giving several hypothetical increases in LIBOR. Now a 200 basis point increase would cost you $540 million which is, I don't know, 65 or 70 percent of the IO. And that's actually net of the caps. So it seems to me that the caps - - I thought they protected you but it seems to me that they don't protect you until LIBOR actually raises all the way to the WAC is that correct?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Of course. Once you get to the cap anything that goes over the cap we are overprotected because - - our presentation is that as rates rise, we shall be - - the losses in the - - in the IO's should be compensated fully in part by the hedging gains. Of course we are talking about the most severe of 200 basis point parallel shift. That will be the ideal situation for us. Now, when you mentioned in hedging losses that they remember the hedging, we have been using cash - - I mean, accounting hedging, we have done everything mark-to-market. Bear in min what happened to Fannie Mae because they had intended to use accounting hedging procedures. And now they are saying that the losses may be $12 billion for Fannie Mae. In our case we'll do our mark to market rate every quarter.

For instance, right now, we have to work from March 31 to make a mark-to-market officially in the quarter. And now the price of oil is rising and something may happen between now and then of the month that you can have a reverse of rates, and then we'll have to do the rates from mark-to-market. That's what has happened in previous years. We have to do a mark-to-market - - we have some quarters where we have extensive gains in hedging and others that we have had losses. But all where we have the corresponding gains in the cash market or the IO's more than that. Because our Company - - we are being increasing our lending constantly for the several years. So that's why - - I mean hedging seems to have business that we have been protected against scenarios [inaudible]. As I mentioned in the very beginning for the year 2003, I mean, expectation were for rates to rise and they went down because of the so-called disinflation or deflation talk that we are in the middle of the year. And then 2004 again, rates were expected to rise significantly. At the end of the year, the 10 year rate was about the same as the one at the end of 2003. And now rates expectations are to go significantly higher. As you no doubt - - again we have a reversal. We have the benefit of doing a mark-to-market from any kind of losses that we have in the hedging account will be reported to the market. By the way, as I said before, those caps they vary from buyer to buyer. And we feel that this is inappropriate to provide a specific information. However, in that you want to note that you see the impact of hedges. For instance, the Company purchased interim rate caps. These are caps that we have purchased - - in [inaudible] As as 4/31/04 We had 2.1 billion of no share amount of interest rate cash and also new ones have been added since then.

Tom Purcell - *Viking Global - Analyst*

Okay, one last question, a couple of times people have asked you about this. And you've talked about additional hedging you've done since the end of the year. Now, presumably the dealers aren't going to give you those for free. So how much does it cost you to further hedge your IO since the end of the year?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, it costs, of course, a - - but, you know that depends on how much of the - - our money or active money productions to quantify the exact amount of that cost is right now difficult. It's difficult to say but, for instance, we are using more 10 year caps and 5 year caps. Of course as you know, you don't have to invest much in those. Again, if the market goes against you you will have to do a mark-to-market and have a loss or a gain. Of course if it goes the way you expect - - go in your favor you'll have a gain. We are hedging those kind of swaps especially 5 year swaps and some 10 year swaps. And of course about this investment, typically we look to have an investment $100 million a year.

Tom Purcell - *Viking Global - Analyst*

Sorry to interrupt.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

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For many purposes.

Tom Purcell - *Viking Global - Analyst*

Sorry to interrupt but why are you using 5 and 10 year caps to hedge an inverse IO whose value is dependent upon the 3 month LIBOR? Why aren't you using short term interest rate options? I mean are those- - must just be too expensive.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

The only thing, for instance, if you want to protect against the next expected Fed raise for June it's already discounted in the markets. That's why our experts in this matter they are saying to us listen; if you have a [inaudible.] Everything will go on. That's actually a comment of Chairman Greenspan. That he mentioned, this must be a short term-aberration. Because [inaudible] 2 years 5 years, everything has been going up in rates. And that what has happened in the market. Every year, it's a different of course security, because the U.S. Treasury is not issuing 30 year bonds anymore for the last 2 years. But anywhere from 2 year, 3 year, 5, 7, 10, give me a 30 year now. Rates are have been going higher after the market listened to Greenspan. So you have a parallel shift in the curve. But even with Euro dollars, for instance, the one year out, at one time, they were going nowhere. For a very short term they were going higher. So it was economic as Greenspan mentioned.

Tom Purcell - *Viking Global - Analyst*

Right. Okay. Sorry I took so much time. Thank you very much for having the call.

Operator

Your next question is from the line of Jay Weintraub of KBW. Please go ahead.

Jay Weintraub - *KBW - Analyst*

Okay. Thank you. Good morning. My questions actually have been asked and answered, thank you.

Operator

Your next question is from the line of Roberto Fernandez of Smith Barney. Please go ahead. Mr. Fernandez, your line is open.

Roberto Fernandez - *Smith Barney - Analyst*

Yes, good morning, gentlemen. All of my questions have been already answered but I do want you guys to make a comment for purposes of people not living in Puerto Rico, about the current condition of the housing market, the expectations in terms of your mortgage originations. And what measures are you taking to maintain the level of mortgage production necessary to maintain your current levels of revenue and on mortgage originations on sales?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Roberto, our housing market in Puerto Rico is very strong. And of course especially in the segment that is our target. Our targets are middle income families, and of course social interest, affordable housing we have a lead of over 50 percent market share in affordable housing. So I that our governments, including this one are sponsoring. We have a need of hundreds of thousands of new homes or homes that need to be improved. One thing that is very significant in Puerto Rico, that we have over 50 percent of homes with no mortgage on it. So that's something - - that's a market that we want to pursue going forward to convince these people that they are not risking their homes if they mortgage. And they use proven financial policies and on budgets and that sometimes, it's better to pay a 6.5 percent mortgage rate than to pay a short-term 30 percent on a personal loan, or small loans that they get up to 5% - - or $5,000. In Puerto Rico they pay anywhere from 25 to 30 percent. So personal loans you have to pay 15 to 18 percent. So even 21 percent on credit cards.

So it's much better for many of these individuals and families to refinance as many borrowers do with us. And they have a more smaller rate, interest rate and also mortgage interest rates in Puerto Rico are in fact I know it is in the States. So it's a - - it's a good strategy for a homeowner to have this type of debt to consolidate and many of them do it. The only thing that we are waiting for is refinancing existing homes. In new homes for this kind of market, we've done very well. We will stay away of luxury homes and second homes. For instance, we rejected a second home project in [Felhago] that was a good project. It sold perfectly well. But we found that for ourselves it was not the type of financing that we wanted to provide. So that development sold very well. Also in other areas of Puerto Rico that we have fine homes, they are considered to be second homes we stay away of this financing. So really, I think that the housing in Puerto Rico, and this type of housing below 150,000 they are selling like hot cakes. [Inaudible] in certain areas, my goodness, the presales are fantastic. We're talking about prices that are very affordable. And This same situation is happening in New York where we are. That we are financing there in Queens, in Brooklyn in the Bronx and, of course, we are not that particularly aggressive in Manhattan, because of the high prices in Manhattan. Over there, the New Yorkers they don't think that the housing market is very hard too. And we continue like that.

Roberto Fernández - *Smith Barney - Analyst*

Thank you. Gentlemen, could you care to comment in regards to current measures that you are taking to maintain the leverage of mortgage production necessary to maintain your current levels of revenue?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, of course we - - I think that we have the marketing force that all institutions they don't have it here in Puerto Rico. We are expanding the marketing for those. We are focusing on the type of loans that we really are looking after. For instance, we don't want to compete so much on a high amount of dollar, let's say $500,000, you have to provide a low rate. We prefer to do loans of $50,000 in which you can charge more and you have a more loyal customer are going forward. So that's our policy to redouble our efforts to expand our marketing in force and right now - - for instance last night, [inaudible] the second largest city in Puerto Rico, are giving incentive to our people in the banking sector to provide more loans to us also. We are expanding into automobile loans and also commercial loans. Those are areas that we are growing.

Operator

You have a question from the line of David Chamberlain of [Atroplet] please go ahead.

David Chamberlain - *Atropolet - Analyst*

Hi thinks for taking this call. Most of my questions have been answered. I guess, finally when you guys think about restrategizing. I'm wondering if you would consider in the future, selling the retained interest and just taking a whole cash gain on sale where you could possibly port fully in some of these loans? Evidently I would argue that the market is not giving you maybe an appropriate value that you would like on that IO. And maybe would better appreciate a more conservative, perhaps, accounting measurement on how you value these asset.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

David of course this is an idea that we are exploring. But bear in mine as Ricardo mentioned to you that the cash returns on these IO's are very high. And I think that the marketing in ways is interesting also the kind of the rates are going higher. And of course we have this kind of reversion of our [inaudible]. And not only us other other financial institutions. So of course if I were an investor I would say this company after looking at where our rates are going, they are going through the roof, to double digits like in 1980 or to what rate are we going forward? So where it is our rates are going to be in a range of anywhere from maybe 2 percent to 5 percent. I think this is a Company to be invested in. Of course you go to the 1980s, double-digit inflation, double-digit interest rates is out of the question. So your point is of course a good one but also bear in mind that this IO they don't enjoy the kind of liquidity that you say - - you want to say mortgage backed securities or any type of other investments. This is a consideration of course depending on the kind of rates that we have because also these IO'S have provided also significant gain in the past. And we we expect that this will level out about sometimes and from there we'll continue making good income on our IO's. But you have your point. And this is something that you have a give and take always in business and you serve something get a benefit well then you lose something else. This is a situation that we have to monitor. But these IO's have been in place for many, many years, and have contributed tremendously to our net

income in the past. So this is something that I think we have it in place on hedging works the way it should work we could have a real return going forward.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

By the way, I'd to like to add that as someone mentioned that the liquidity of that market of the secondary market for the IO is not that much. However, in the past the Company has been able to sell its own gross IO's in private transactions and in all of those transactions the Company was able sell the IO's at a price or at a value higher than what we had it booked in our books.

David Chamberlain - *Atropolet - Analyst*

Okay. Fair enough. Thank you so much.

Operator

You have a question from Darius Brown of Indica Partners. Please go ahead.

Darius Brown - *Indica Partners - Analyst*

Most of my questions have been answered but I just wanted to reiterate the observation that the best thing you can do for your shareholders now is to try to execute a significant sale of the residual assets. And even if it's at a modest discount that would go a long way to verifying your internal valuation of that asset. And then further I would just like to reiterate that it seems like the market is telling you that the days of non-cash gain on sale accounting are not going to be valued as they once were. And an on-balance sheet model is going to be necessary. Thanks.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Okay. Thank you.

Operator

Next question or comment is from the line of Gerald Caminski of Berger Berman. Please go ahead.

Michael Caminski - *Newberger Berman - Analyst*

This is actually Michael Caminski. We are all here together. First off we just want to make an observing or comment that it would be in the interest of transparency and with respect to the last caller as well, we would recommend revising the confidentiality agreements referred to earlier with respect to any advice you've been given on valuation for the IO And publishing them in a public forum. That would be our first recommendation. Secondarily we have a question would would like to follow up on an earlier response having to do with this Hibernia report and a reply or reaction to the Hibernia report dated March 8 which was roughly a weeks ago. Which is also more than 30 days in advance of the expected earnings release. The comment number 6, which apparently some question was asked about earlier, which states, "the Company has previously said it expects to meet or exceed consensus earnings estimates. So we believe the analysts new revised estimates are too low." It is our understanding, A., that you are referring to comments previously made at the Brean Murray Conference in New York City which was publicly Webcast. That would be our first comment. We would like verification of that. And then secondarily, because you have not issued any revision to that number 6 comment, which we took as a reaffirmation of comments that you made at the Brean Murray Conference, we would assume as we do assume that there's been no material change to that comment in the last 10 days.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

I was the one who said the statement on the Brean Murray Investor Conference, our response to a question which as you said you're right in that was in a Webcast live and later recorded for the market to see or view live through the Internet as well and through our Website. So that was referring to a public comment. Nothing has changed in terms of the fundamentals of this Company. Nothing has changed since then.

Michael Caminski *- Newberger Berman - Analyst*

Thank you very much.

Sammy Levis *- Doral Financial - Senior EVP, Treasurer*

Okay.

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

I would like to add of course that this depends on the volume of our loans going forward, something that we cannot in absolute terms guarantee. And of course, in the hedging techniques that we have in place to continue working. So of course all these forward-looking statements are based on models that we are running and depends on the accuracy of this model.

Michael Caminski *- Newberger Berman - Analyst*

We understand and appreciate that. And anything can change based on the values at the end of the quarter of one day. But there is nothing that's happened today.

Sammy Levis *- Doral Financial - Senior EVP, Treasurer*

No, as you mentioned, not only that, I mean you never know what could happen, we have God forbid another 9/11 event and the Fed would have to raise rates we never know. After I made that statement on that public forum, nothing has changed my theory in terms of the fundamentals of this Company as of today.

Michael Caminski *- Newberger Berman - Analyst*

Great. We were would just reiterate we hope that the counter parties with whom you sound signed this confidentiality agreement will agree given the very great uncertainty in the marketplace to let them - - their names be publicized. And in fact for them to communicate with people who want to ask the various very important technical questions about how valuations are achieved. And in that regard can you confirm what I thought you said which is that you were using in valuations current coupon Fannie Mae by given date plus 300 basis points as your discount?

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

Yes.

Michael Caminski *- Newberger Berman - Analyst*

And as you said earlier because of that there will be changes every quarter because the current coupon Fannie Mae will in fact fluctuate every 3 months. Is that correct?

Sammy Levis *- Doral Financial - Senior EVP, Treasurer*

Yes, that's correct.

Michael Caminski - *Newberger Berman - Analyst*

Okay. Thank you very much.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Thank you.

Operator

You have a question from Aio Okasana of UBS. Please go ahead.

Aio Okasana - *UBS - Analyst*

I guess just going back to this question of - - well actually I have 2 questions, first one in regards to just loan production, I noticed from calculations I'm doing that production in Puerto Rico actually for Doral has been slowing over the past 2 quarters. The numbers I have show that it slowed to 1 percent quarter on quarter gross in 2Q '04. 1 percent quarter on quarter gross 3Q '04 and was actually down 5 percent in 4Q '04. So it is seems like although you do have a record loan originations a lot of that is coming from the U.S. side rather than Puerto Rico. And since Puerto Rico is your high gain on sale margin business I was just wondering if you could give comments on what happened over the past 2 to 3 quarters that Puerto Rico's loan origination is slowing?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Historically, we have about 30 percent of the U.S., in the U.S., that percentage has remained sustained, maybe going somewhat. But we haven't really seen a decline in originations in Puerto Rico.

Aio Okasana - *UBS - Analyst*

I'm sorry?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

We haven't seen a decline in originations in Puerto Rico.

Aio Okasana - *UBS - Analyst*

Well, the numbers I'm running here just based on your disclosure every single about loan production if I split those numbers out between U.S. origination and Puerto Rico origination on a quarter to quarter basis: it actually shows that your origination fourth quarter '04 for Puerto Rico was about 1.278 billion but in third quarter it was 1.35 billion. And this is all based on information you have in your K.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

You are looking at it from quarter to quarter?

Aio Okasana - *UBS - Analyst*

Yes, from quarter to quarter.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Bear in mind that December, I mean always December is one of the worse month of the year because of the holidays. Our fourth quarter is not the best one, in number percentages.

Aio Okasana - *UBS - Analyst*

What about your second quarter and third quarter where you had 1 percent quarter over quarter growth in Puerto Rico?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Okay. Are you taking into account that about 8 percent of the home sales purchased are in Puerto Rico.

Aio Okasana - *UBS - Analyst*

Sorry?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Are you taking into account that 8 percent of the home sales purchased are in Puerto Rico.

Aio Okasana - *UBS - Analyst*

Yes. I am, I do have those numbers. I'm just backing into what your Puerto Rico numbers should have been much. It seems like second quarter '04 over first quarter grew 1 percent, third over second quarter grew 1 percent. Fourth quarter over third quarter in Puerto Rico, down 5 percent. And I guess the question I'm asking is this more of a trend because of rising interest rates or was there something unique in second and third quarter? Because I do think there was more significant hurricane season this year.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, let me explain to you when of course you are comparing dollar amount with dollar amounts. Internally, what we compare is number of loans closed. Why? Because when you have a big financing boom because rates are coming down significantly, a happened in the year 2003, for instance. Many of - - we have bigger loan amounts coming to us also, like loans of 300,000, 500,000, even loans up to 1 million or more. For us the profitability is not in those type of loans because of so much competition. And going to the higher people in the pyramid. But - - we have for instance competitors that they do additional amount of loans both based on dollar amount not on number of loans. For us the number of loans are more significant in the sense of: as I told you previously, we prefer to have 10 loans of $50,000 than 1 loan of $50,000 - - I mean of $500,000 although servicing of course is more expensive, the borrower of $500,000 is a typical borrower that will shop around looking for the best offers and the bottom line is not there. You have to give the very lower interest rate if you want to get the business. In the more low middle income family and middle income they are not shopping around so much. So we can charge a little bit more on of course this type of loan of 50,000, 75,000, 100,000, are not pursued as aggressively by all institutions. And the same is happening, for instance, in New York City with our bank institution with commercial loans, the smaller commercial loans are not so heavily pursued by other competitors.

Aio Okasana - *UBS - Analyst*

I guess I understand that point but my concern is that the gain on sales, are calculated and not off the number of loans but the full value, the dollar value of the loan sold. And if that loan is down --

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Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well the dollar amount of the loan are really can't be put together for IO's. for instance, this type of loan of 300,000, 400,000 we will not put it there. So this is the type of loan of in a way, are not put together into an IO. What we are doing is packaging loans with an average loan amount that is substantially lower that this type of loans that very competitive, that brings you dollar amount volume with no significant return. And that's happened with other institutions in Puerto Rico and also in the U.S. We are focused on the nonconforming loan, the low balance, low [LTV] loans that close, that our target, our focus is there. Every time that we have loans of 300,000, 500,000, we don't make money on those loans except for services.

Aio Okasana - *UBS - Analyst*

Okay. Thank you. The second question I had, again, going back with the IO's and needing more clarity. I know the assumption right now is the prepayment speed based on your current estimates and numbers you are seeing at systems and things like that is 7.2 percent. But over the past 3, 4 years, that number has bounced around so much depending on the interest rate environment that I guess just going forward, how we are to be comfortable that it won't go up again or down?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

It may go up again or down. But it's like in Bloomberg you take any, coupon - - Fannie Mae coupon or Ginny May, they will provide you differing [inaudible] depending on expectant life. And sometimes we have a lot of prepayment on the 6 percent and then the rates go up, you have a - - duration would be longer. So it's a changing, a moving target.

Aio Okasana - *UBS - Analyst*

But based on that comment then if the weighted-average life of these loans is life is 7 to 8 percent; in regards to the prepayment speed you used shouldn't you have some type of long-term outlook to value these things for IO purposes rather than this number changing every single quarter?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Of course but within that you also, the PSA is a moving target. That you can write, Ricardo every quarter wants to do a mark-to-market based on this moving target and you have not only us; other companies like is see here [Sender Mortgage], SunTrust, Wachovia, CountryWide, Washington Mutual, Wells Fargo, it's not a version of a moving target. That's an estimate based on our most recent experience. Both of it happening in year 2003 we had the so-called disinflation. Of course we had more prepayment because rates went substantially lower in a short period of time. So you look for instance at 2003 we have a lot of more prepayments because of of course we have a situation that was abnormal of rates coming severely down like the 10 year rate coming down to 3.11 percent. These are situations that may happen that may change the model that you have going forward. We are looking now for rates to go higher. That's what most participants in this market are expecting. Short term rates to continue going higher and also mortgage rates to continue going higher. That's what the expectation is. I think that they are based on what the Fed is doing and what the Fed has announced that they are doing. They are going to be doing.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

This is done every month. And remember that we use market rates to determine the [inaudible] so their inflation with those rates are - - there's going to be fluctuations in the value of the IO.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes. We do it internally every month and. of course, externally every quarter.

Aio Okasana - *UBS - Analyst*

Fair enough. Thank you very much, gentlemen.

Operator

You have a question from the line of Tom Monaco of Mours and Cabot Capital. Please go ahead.

Tom Monaco - *Moors & Cabot - Analyst*

Hi, Sammy. I have a question regarding the MSR valuation relative to R&G. I keep getting an awful lot of questions surrounding that and your MSR. valuation is higher than R&G. and also [Popular]. I was wondering if you could give clarity with respect to that and how you value your MSR versus an R&G and a [Popular]?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Let me ask a question. Are you talking about the MSR or the IO?

Tom Monaco - *Moors & Cabot - Analyst*

The MSR.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Yes, as I mentioned before the MSR is - - we use a range of 230 to 150 for the initial capitalization of the MSR. And we value the MSR with an external, third party player on a quarterly basis. Doing, the tough years I guess we have been recording impairments in the MSR portfolio. That's why you see that our MSR has been - - although my portfolio has been going up. Still the capitalization of the MSR is not going up in tandem with the increase in the portfolio. We- - if the MSR is also producing cash we stand on the valuation and we hope the resolution is resolved.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

And by the way these evaluations that is done by a third party independent valuation. And we just don't actually in this system we don't use any internal valuation. I don't see that compares, this portfolio might have different type of loans within the portfolio.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes. Remember also that this portfolio has prepayment - - prepayment penalties. The nonconforming has prepayment penalties on their [inaudible] and fees [inaudible] portfolio. That also are considered in the valuation.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

And by the way our portfolio is the youngest one in terms of most of the big increases has been in recent years. One of the institutions that you mentioned has a very old portfolio from a mortgage bank that they acquired many years ago. So you have to compare apples-to-apples. And by the way we are known to have the lowest prepayment of - - in Puerto Rico.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

And you'll see that prepayments are going down, the coupon of the portfolio is going down which means that the portfolio is going to last more.

Tom Monaco - *Moors & Cabot - Analyst*

Okay. But the disparity between yourselves and an R&G I think is close to, it's about I think it's nearly 30 basis points. Is it the mix of assets? Is it more Puerto Rico based assets than R&G? Is it, you mentioned the mix of type of loans, is it a geographic issue? Is it a type - - what type of loans and things of that if we can get a bit of a better breakdown here?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I don't know the portfolio of the other company. [inaudible] servicing outside Puerto Rico which tends to be overvalued. So I really cannot comment on that portfolio because.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

All of these loans have different - - I mean some of them may be - - in our case and I cannot speak for them, in our case it's composed of FHA, VA, conforming and nonconforming. In all those 3 products, they enjoy a very low prepayment speed, lower than the average. Also you have these funds that portfolios are older than us. I mean our portfolio may be younger. And also you have the conclusion that some of that other portfolio may contain U.S. servicing, which is actually 100% - - or not necessarily 100% but close to 100 percent of our servicing portfolio consists of Puerto Rico. The other 2 institutions that you mentioned do have significant amount of U.S. based servicing loans.

Tom Monaco - *Moors & Cabot - Analyst*

Okay. Would it be possible for you to disclose what the, I guess the weighted-average servicing retained is?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Servicing?

Tom Monaco - *Moors & Cabot - Analyst*

The weighted-average servicing retained, what kind of, I guess fees are you receiving?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

It is in the range of 31, 32 basis points.

Tom Monaco - *Moors & Cabot - Analyst*

Okay. All right.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

And that does not include ancillary fees like prepayment penalties and other types of fees that is generated by the servicing portfolio.

Tom Monaco - *Moors & Cabot - Analyst*

What is your mix of Puerto Rico MSR's versus U.S. MSR's?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

It is over 95% is Puerto Rico MSR.

Tom Monaco - *Moors & Cabot - Analyst*

Great.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Actually I think it's even higher than 95.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Remember that the U.S. loans that we are buying we just buy the loan not the servicing.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

By the way I just got that number here from the 10K, 98 percent

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Tom Monaco - *Moors & Cabot - Analyst*

98 percent.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

And that is not the case for the other 2 institutions.

Tom Monaco - *Moors & Cabot - Analyst*

98 percent is Puerto Rico based MSR's?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Right.

Tom Monaco - *Moors & Cabot - Analyst*

And Sammy, you and I had talked about a month ago about the valuation of the MSR's could potentially be higher based on the prepayment penalty. Can you go into that a little bit?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

The prepayment? The valuation going higher because of the prepayment.

Tom Monaco - *Moors & Cabot - Analyst*

The valuation of the MSR's could be potentially be even higher than what it was based on a the prepayment penalty.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

I think there's a misunderstanding the MSR, the MSR valuation is already confused with the prepayment penalty.

Tom Monaco - *Moors & Cabot - Analyst*

Okay.

Sammy Levis - *Doral Financial - Senior RVP, Treasurer*

And by the way I don't believe I have ever said such a statement.

Tom Monaco - *Moors & Cabot - Analyst*

Okay. My misunderstanding, Sammy. That's all the questions I have. Thank you.

Operator

You have a question from the line of Scott Froehlich of ING Investments. Please go ahead.

Scott Froehlich - *ING Investments - Analyst*

In your prepared remarks you talked about a mix between fixed and floating mortgages and how that affects the prepaids. Prepaids. Can you talk about how that mix has shifted over the last couple of years? And then what the prepaids are for each?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Could you repeat that again? We are not able to hear well.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

A little bit louder, please?

Scott Froehlich - *ING Investments - Analyst*

Hello?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

We didn't hear the questions.

Scott Froehlich - *ING Investments - Analyst*

If you could just talk about the mix between fixed and floating mortgages and how the prepaids differ.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Oh, the floating mortgages of course we have been doing the most and of course in the fixed IO's without that kind of a great income. And that's why we are being wary and some of the IO's are switched floating IO's by refinancing. In other words we don't provide the incentives in refinancing loans. that part of IO's are to our marketing force. While we compensate our marketing force for refinancing loans in the fixed IO's

especially in the ones that were created a number of years ago in which our spread is very narrow since inception. So that's why maybe the fixed IO's we are refinancing them on more rapidly than the floating IO's.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

We think that there has been more interest --

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

In the IO's in the floating IO's.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

In the floating IO's.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Maybe in the future we will have to come back to the fixed IO's again.

Scott Froehlich - *ING Investments - Analyst*

Thank you.

Operator

You have a question from the line of Stephen Davidwicz of First Security. Please go ahead.

Steven Davidwicz - *First Security - Analyst*

Yes, hi, Salomon, hi Sammy. I guess I would like to ask this question. And put it in the context that as far as I've known you've been a great company for many years, consistently growing your earning, consistently growing your dividends, consistently transparent, responsive to the shareholders. So during this period of time maybe just take another chance for either or both of you to just comment for the retail investor as he contrasts the comments recently by the couple of analysts and those specific concerns. And then how to reconcile that with your long track record of just being a very consistent executing Company and just an opportunity today to just throw out comments for those retail investors?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I think if I were a retail investor I would take a look at the recommendations of my stockbroker and others. This sometimes stockbroker may be right or may be wrong and, of course, the transaction of the stock - - you mentioned the performance of this Company throughout the years. We have been around 33 years now. We have been around in the 1970's with the higher rates, 1980's with extremely high rates also 1990 and now in the year 2000 and up. So we have different scenarios we have been profitable every year. Of course we have phenomenal record earning for a number of quarters. And right now because of what happened in the last quarter is some people lose faith. I mean some analysts or whatever but we have been there, you mentioned for a number of years, this Company is growing very fast. We were a not 10 years ago in terms of a bank institution now.

We have a good market share now of the market and growing in Puerto Rico. As Sammy mentioned before I went to [inaudible] in the south part of Puerto Rico last night. We visited there we have young people very energetic and able to grow within the Company and make this Company grow faster. We are also in the insurance of growing very fast as a fee income based Company. We are in New York where we are very happy with what's happening in New York City with our bank. We are doing very well in [inaudible]. This is a Company that this is growing. And we have a net worth of that we never have before. So if we were a target for instance of just [inaudible] of a purchase from a new institution they

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would see that we have a strong Company with a kind of a structure, financial structure and also this is a structure that we didn't have even 5 years ago. And that's our purpose is of course if you take any company, any financial company, any great company, any big company in the U.S., we have our ups and downs. And it seems that the market now is giving us a down. But price distortion will reflect sometime the attractiveness for retail acquired window. And again any investors that have invested in this Company in any given year in the end, in the few years we still have they still have outperformed many of, most of the U.S. stocks, all the stock in the U.S. And of course, more than any other financial institutions in the U.S. In the past. So maybe the market is giving retail buyers an opportunity to get into this Company. But of course this is something that doesn't correspond to comment because I'm the CEO. But the price retail - - at what level of price people will be willing to buy this Company aggressively again.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

If I may add this is a situation last quarter as we say of the movement raise in a very unusual manner. Historically there have been 2 or 3 times where the this type of environment that you saw and we we had a situation with the IO. The Company is making adjustment trying to fix the situation. But other than that if you put that aside for a second the momentum of this Company remains quite strong. And our mortgage banking business is doing well. Our commercial bank is doing well and our insurance business is doing well. And as we said before, in next quarter when we are expecting more loan originations, the commercial banking loans to grow at record pace and the insurance also to grow at a record. So if you put the IO issue aside for a second something that in way it is a temporary nature because eventually the U.S. cannot continue to have this type of interest rate environment. And so I mean the momentum of this Company continues very strong and if you put that aside you should expect better years to come.

Steven Davidwicz - *First Security - Analyst*

On behalf of everyone I thank you very much for having this conference call.

Operator

You have a question from James Shanahan of Wachovia. Please go ahead.

James Shanahan - *Wachovia Securities - Analyst*

Thank for taking my call. One was kind of a high level question as a follow up. The Company said they believe that Puerto Rico mortgage production would rise in 2005. Is that correct?

Solomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes.

James Shanahan - *Wachovia Securities - Analyst*

And you still expect that 50% of production will be refinance activity. I assume that's also true, that's been the historical.

Solomon Levis - *Doral Financial - Chairman, CEO, Director*

Right. Yes.

James Shanahan - *Wachovia Securities - Analyst*

So I guess an earlier caller who cited the historical servicing portfolio, CPR's relative to your outlook for a lifetime speed 50 percent lower at 7.2 percent. And I see a disconnect here. You have mortgages originated and sold expected to prepay much slower but 2005 mortgage production is

still substantially driven by refinance activity. What is the difference between the production that you expect and the production that you've already originated and sold?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, because, bear in mind that we are in new construction, of course new construction at our Company new loans. And what we are doing is getting more loans as I mentioned before. We have over 50 percent of housing in Puerto Rico from 40 to 50 percent of housing are without any mortgage. So, for instance, 2 weeks ago I got together with the Association of Retired People in Puerto Rico, they have over 60,000 people. And many of these folks, they don't have any mortgage on their home. And we are trying to sell the reverse mortgages to them and this is a completely new line of business for us and giving seminars for people that they have - - they need to have some kind of additional income while they are alive. And you will see in the kind of new marketing effort that I mentioned earlier in this conference call that we are doing and we continue to more and having to do with this type of properties. In which we don't have any, any liens. Of course a as you mentioned in loans at our floating IO's we try to preserve that not to push those cases. But anyway as the case of 7.2 percent of prepayment you are talking about in there final [inaudible] in new loans that you can do giving us 7.2 percent from that portfolio. But our idea is to continue growing. And I think we have a lot to grow in new housing, a lot to grow in re-fi loans that belong to the competition, in a new line of loans in homes that have no mortgage at all. So I tell you that's why we can continue growing.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

And also remember that we are different than in the U.S. For instance, typically although we have a higher refinancing percentages than the mainland the refinancing in Puerto Rico is lower because most of it is for consumer consolidation of debt that happened every so - - 6 or 7 years. Of course not all these people refinance at the same time. So they are financing in cycles. And also although we are trying to avoid refinancing our own portfolio the one behind the IO's we are also refinancing other portfolios that are not on our books. So putting those 2 together they just don't go alone.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

We have a lot of portfolio that is not in the servicing portfolio that is not related to this growth in rates that we can refinance at any time.

James Shanahan - *Wachovia Securities - Analyst*

Now what percentage of your production is new housing, is it like 10, 20 percent, - - 20 percent?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

It would be from 15 to 20 percent depending on the particular month.

James Shanahan - *Wachovia Securities - Analyst*

And then regarding the reverse mortgage--

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

By the way also --

James Shanahan - *Wachovia Securities - Analyst*

-- the issue, I didn't realize this was a new market for you but the total dollar value of reverse mortgage originations in 2004 in the mainland was $6 billion in a market that's $2.7 trillion. This product has been around for awhile. It's a primary an FHA VA product and it doesn't really have

very wide consumer acceptance here in the mainland. What do you think the market size is for reverse mortgages in Puerto Rico? Is it $100 million, is it 200 million?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I cannot tell you right now because we are in the beginning of it. I know you are right, this product has not been very accepted in the U. S. In Puerto Rico some other homeowners invited us to revisit this, I think that the way of selling this product is to get together with the person that is already an older person, a retiree and also with their family and explain this kind of product. And the President of the Association of Government Retirees he made the comment with us that to have a big seminar and invite these people because we read the statistics and there are a lot of people that they receive less than $500 a month for living with the pension and also a big chunk of people that receive anywhere from $500 to $1,000. But your point, you are right, that's something that we want to break. To do loans for these people that number one they need it and I think that we can also help them. In what kind of volume we can do I think it's too early to tell. But that's something for us is a challenge and something that we will start doing it right away.

James Shanahan - *Wachovia Securities - Analyst*

Since you brought it up I wanted another follow-up question, regarding the new housing market, I was reading in one of your newspapers down there that a local developer talking about construction costs and materials costs rising significantly, land costs are rising. And he was nervous about the impact of even modestly higher rates. And that a lot of the construction costs are really running so high now that home prices might be getting out of hand for, in this low to middle income segment. Are you seeing that? Is that - - can you comment on that?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Well, let me tell you of course, for instance, if you take some sections that's very true. For instance if you take [Candalgo] there is a section of hotels, tourists and also residential, the price of land has skyrocketed. We are talking is similar to Manhattan. Of course what we have seen for instance if you take [San Tourisa] that this area adjacent to [Candalgo], this area was like a neglected area. And then the government, what they did, they started renovating, I mean buying all this kind of land in this area and giving it to private developers and it's a great winner. This is area of [San Tourisa] that this is area only like less than 500-meter from [Candalgo] it's a very luxurious area. For instance we have a commitment with the Governor and also the majors of the [inaudible] to renovate the core areas similar to what they did in the area in the [inaudible] different municipalities to give you the Major of [Kawa] one important and very fast growing city has been calling all the bankers to help him to renovate and put there thousands of new units by the municipality providing the land for free or at a very low price.

So private land is expensive, it's becoming more expensive in certain areas. But you have the Government of Puerto Rico and you have the municipalities that they own still a lot of land and they are accommodating to prices that make the new housing very affordable. On top of that you have the affordable housing program that have been expanded to $90,000 in which the government will provide incentives and subsidies to people, poor people and low, middle income people who are buying these homes with these sources and giving such from the Federal Government. So this is an area that are growing faster and faster. And more municipalities they have land that they can give the developer at a very reduced price and in some instances as I mentioned to you, for free, in order to attract people to move to this smaller municipality. That's my answer.

James Shanahan - *Wachovia Securities - Analyst*

Thank you. Looking at the question and a lot of these IO question have been asked. But I had one here regarding the prepayment speed assumptions that have changed so considerably over the last few years, from 13.5 percent, 13.3, 13.3, 18 percent, now 7.2. But I guess I still don't really understand that the expected weighted-average life of either the retained interest, hasn't really moved around that much. That even at 13, 18, 7.2, it's still a considered to be or expected to be 4 to 8 year average life asset. And at a prepaid speed like 18 percent, it doesn't even, mathematically make sense that it would be a 7 year average life asset. It seems to be like less than 4. Can you explain why that - - the expected average life never changes or very rarely changes when the prepayment speed assumption changes?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Well, you will see that valuation's remaining life going out by one year, in '04, there was not a reduction in the prepayment speed. Keep in mind that this is an asset --

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Salomon Levis - *Doral Financial - Chairman, CEO, Director*

It went.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

We don't want to extend - - we want to amortize these out faster rather than slower.

James Shanahan - *Wachovia Securities - Analyst*

But the amortization expense that you are reporting on your IO's has been pretty steady at $25 million or so per quarter. And this is true when the asset is 860 million same as it is when it was 578 million. And your amortization expenses isn't changing the IO keeps getting bigger and bigger. So you are saying you want to amortize it faster. I don't see that?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

We're passing a an incentive - -

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Yes amortization is related to the prepayment speed assumptions that we use. So you have to expect changes in the amortization when you have changes in the prepayment speed.

James Shanahan - *Wachovia Securities - Analyst*

Okay. The gross yield on IO's has been declining pretty consistently over the last few years. It used to be in the mid 30% range and it was in the high teens, I didn't calculate it for the 10(K) but what is the relationship between the yield on the asset and the asset's value? Is yield a consideration in determining value?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Well you have to do the calculation that if the IO rate increase, the spread that we're getting on the IO is shrink. So that is [inaudible] yield is going to be down. However, the life of the loans of the IO value is going to be expanded because you have a lower weighted average coupon, you have a longer life expectancy. So you are going to receive less or you are going to receive less for more time.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Did we answer your question Jim?

James Shanahan - *Wachovia Securities - Analyst*

Yes, it does. And if we have time for just one more. I know you've been very generous with your time.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Thank you, again.

James Shanahan - *Wachovia Securities - Analyst*

The net interest margin, there's a Table X in the 10(K), interest rate sensitivity, at December 31, Doral reported that for 100 basis points, 200 basis points increase in rate would lead at a reduction of 11.8 or 17.3 percent in net interest income respectively. At September 30 these same plus 100 to plus 200 basis points scenarios would have led to an increase in net interest income of 2.6 and 4.8 percent. It's a big change in my opinion. Do you, can you discuss how you model that and is it just the shape of the yield curve that caused that to change?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Yes, [inaudible] the changes are [inaudible]model. Including more [inaudible] of the loan product, different assets securities like [inaudible] opportunity to [inaudible] interest rate on the [inaudible]. In addition the new [inaudible] [inaudible] spread [inaudible] the ability of the [inaudible] to determine when the call auctions are [inaudible] [inaudible] would be exercised.

James Shanahan - *Wachovia Securities - Analyst*

Do you use option adjusted spread or a more static analysis?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

We are using a static analysis in the past. And we are switching to an option adjusted spread right now.

James Shanahan - *Wachovia Securities - Analyst*

Have you switched to an option adjusted spread analysis for IO's and MSR values?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

No.

James Shanahan - *Wachovia Securities - Analyst*

Okay. So tou are still valuing that on a static basis?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Yes.

James Shanahan - *Wachovia Securities - Analyst*

I appreciate your taking my call, yes.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Again, by the way the Company to account the flow of cash which is 2.5 billion, with 60 percent of that into static MBS's.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

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And also more leverage that we could do.

James Shanahan - *Wachovia Securities - Analyst*

It doesn't consider the cash, the potential for cash reinvestment, does it not?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

No, it does not.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

More leverage that we can do in the Company.

James Shanahan - *Wachovia Securities - Analyst*

And more leverage, right exactly. Okay. Thank you very much.

Operator

You have --

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

One more question [inaudible] because right now it's - - we have been around like 1 hour and 40 minutes, right? I would say maybe one more question or a couple of questions.

Operator

You have a question from the line of Emanuel Sabong of Rockefeller. Please go ahead.

Emanuel Sabong - *Rockefeller - Analyst*

Hi, my question has to do with the prepayment fees. Why has prepayment --

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Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I'm sorry, could you raise your voice, please?

Emanuel Sabong - *Rockefeller - Analyst*

Sure. Why have prepayment speeds changed so much over the last year but weighted average life is relatively constant? I would just like to get some clarity on that?

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

Well, you see weighted average it's related more or less to the amortization period that we use for the IO's. While the speed is based on the actual prepayment that we have in the portfolio of the loans underlying the IO's. Which is basically a nonconforming portfolio.

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

The weighted-average, weighted-average would be longer than the, would be lower than - - Actually

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

in December you see the weighted average life was extended 1 year from 7 to 8 and the prepayment speed down. And we were using last year almost 7 - - it went down been 7 from - - the weighted-average life of 7 to 8. And as we mentioned it was decreasing prepayments we saw 18 percent to 7.20.

Emanuel Sabong - *Rockefeller - Analyst*

I'm just trying to get a feel for - - prepayment speeds have changed so dramatically - - dramatically slowed, why a small impact on weighted-average life?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Because this is as you know is the amortization of IO's.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

This is remember the remaining in years is the [inaudible] what we use for the amortization of the IO's. And the PSA is basically a function of the embedded in the count [inaudible]. I mean the value of the IO.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

What will happen a more extended weighted-average maturity than the amortization should be longer.

Ricardo Melendez - *Doral Financial - Exec. VP, CFO*

I mean a longer right now. It went to - -

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

1 years. It would be 10 years [inaudible] would be more.

Emanuel Sabong - *Rockefeller - Analyst*

One more question. Just a simple or yes or no question. If your share prices is at the same level in a month, will you ask the board to authorize a share buy-back?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I'm sorry, can you repeat the question, please?

Emanuel Sabong - *Rockefeller - Analyst*

If the share price is, if your share price is the same in a month, will you ask your board to authorize a share buy-back?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

I cannot answer you. I mean categorically right now but - - if we have a downwind and also a small downgrade and they are hitting the price of it still, of course it will be very inviting for us to consider that possibility. It will be our job to give this idea much issue.

Emanuel Sabong - *Rockefeller - Analyst*

All right. Thank you.

Operator

Would you like to take one more question, gentlemen?

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Yes, please.

Operator

Okay. Your final question is from the line of Neil Abromavage of Deutsche Bank. Please go ahead.

Paul Nilnick - *Deutsche Bank - Analyst*

Hi, it's actually Paul [Nilnick] on Neil's behalf. One question we had just with regard to the discount rate that you use to value the IO, in 2003 it was 9 percent and in '04 it was 7.63 percent. I think you said at the top of the call that previously you had a floor in place of 9 percent.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

Right.

Paul Nilnick - *Deutsche Bank - Analyst*

Can you give us a better idea of why you changed your policy to get rid of that floor?

Sammy Levis - *Doral Financial - Senior EVP, Treasurer*

Because bear in mind that we are using a benchmark that is a mortgage loan benchmark. And very bear in mind that rates went down significantly. So at that moment we saw that it was not proper to have that floor. I mean that floor came from many years ago.

Salomon Levis - *Doral Financial - Chairman, CEO, Director*

We didn't change the policy in the current policy it says that you can go below the floor, you can see it for the market is there for a number of loans or whatever. You are allowed to do that. We only did that - - some companies they have remained at 9 percent forever. Even when we were giving a 12 percent discount they were at 9 percent. I think it's not - - it doesn't represent fairly the price or the value of the IO's to have a like a fixed rate always. And I think of course as rates move up as everyone has expected also it will go again the discount.

But really the 2, parts will move the price or the value of the IO's more of the spread. And that we can enjoy in our IO's. And also the duration of the prepayment speed that we will have. There will also be 2 principle items. In a way this discount is not the of the 3 is not the most important item. Anyway, as we have mentioned before that other companies that in the year 2000 they use a 7 percent discount and the year 2003 they mentioned a discount from 5 to 15 percent, listing our - - in our case we have a formula to stand back. Also we are different from people for instance you have another institution like WAMU that WAMU they say that the discount rate is in 2003 was from 3 to 6 percent and also in 2004 it was 4.30 percent. This is WANY. So you have different lenders in the U.S. making different assumptions with the rate. 10 percent. Washington Mutual 4.30 percent, Wells Fargo 10 percent. So everybody has a different ways to arrive at the discount.

But the use of the 9% rule was discontinued because monetizing such as floor could not be justified longer in this kind of low interest rate environment. Because when it was created is was before 2001 when we have this version of 9/11. It was a creation, a policy created before. But in that policy it would also allow to go below the floor if the market we would consider the market shouldn't be there for 9 percent. We think we have the formula. Our formula, as Sammy mentioned, will adjust upward or downward depending on the benchmark.

Paul Nilnick *- Deutsche Bank - Analyst*

Okay. Thank you. That's very helpful. And just to make sure that I'm understanding your sensitivity table correctly if you had used a 9 percent discount rate the way I'm reading that would be somewhere closer around the impact on fair value of a 20 percent adverse change so that would be roughly a $16 million difference?

Ricardo Melendez *- Doral Financial - Exec. VP, CFO*

Yes. If you go to page 39 you will see the adverse change in the discount rate. A 10 percent adverse change in discount rate would give you 31 million impairment. And a 20 percent adverse change will give you a 60 million impairment.

Sammy Levis *- Doral Financial - Senior EVP, Treasurer*

That's pretax.

Ricardo Melendez *- Doral Financial - Exec. VP, CFO*

Yes that is pretax.

Paul Nilnick *- Deutsche Bank - Analyst*

And that's pretaxed.

Ricardo Melendez *- Doral Financial - Exec. VP, CFO*

And without changing any other assumptions. That's an isolated change just in the discount rate.

Paul Nilnick *- Deutsche Bank - Analyst*

Thank you very much.

Salomon Levis *- Doral Financial - Chairman, CEO, Director*

Okay. So we appreciation your participation and questions. We trust that this call was a useful exercise to address your inquiries directly to management. And look forward to participating in future conference calls. Thank and have a good day.

Operator

Ladies and gentlemen, this conference call is available for replay from 9:00 Eastern Time tonight until midnight on March 30. You may reach this call by dial 1(800)475-6701, using the access code of 773968. The number again is 1(800)475-6701 with the access code of 773968. If you are dialing internationally the number would be 1 for country code, 320-365-3844, again with access code of 773968. That does conclude your conference for this morning. Thank you very much for using AT&T executive. You may now disconnect.

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